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Supreme Court, U. S.
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73-1432
No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1973

GEORATOR CORPORATION, *Petitioner*

v.

UNITED STATES OF AMERICA, *Respondent*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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PRESS OF BYRON S. ADAMS PRINTERS, INC., WASHINGTON, D. C.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

The Georator Corporation, your Petitioner, prays that a writ of certiorari issue to review the Judgment of the United States Court of Appeals for the Fourth Circuit, entered in the above cause on October 2, 1973.

OPINIONS BELOW

The Memorandum Opinion and Order of the United States District Court for the Eastern District of Virginia is not reported, but is presented as Appendix A. (Infra page 1a).

The Opinion of the United States Court of Appeals for the Fourth Circuit is presented as Appendix B hereto. (Infra page 4a).

The Order of said Court of Appeals amending and correcting its Opinion and Judgment is presented in Appendix C hereto. (Infra page 10a).

The Order of said United States Court of Appeals denying the Motion for Rehearing filed therein is presented in Appendix D hereto. (Infra page 11a).

JURISDICTION

The jurisdiction of this Court is invoked for the reason that in the opinion of counsel, the United States Court of Appeals for the Fourth Circuit decided an income tax question in a manner that is in conflict with decisions of this Court, as well as improperly classifying the funds disbursed as a capital expenditure.

(i) The United States Court of Appeals Opinion was filed October 2, 1973, and the Amendment of that Opinion was filed on October 26, 1973.

(ii) Petitioner's Motion for Rehearing was denied on December 26, 1973.

QUESTIONS PRESENTED

This case presents the question of whether for federal income tax purposes fees incurred by the petitioner while resisting an attempt to cancel a registration of its trademark, may be deducted annually as an ordinary business expense, or whether it should be treated as a capital expenditure.

Stated differently, must the legal costs incurred in resisting the cancellation of a trademark registration be treated in the same manner as if it were the cost of the original registration?

STATUTES INVOLVED

That the statutes involved in this proceeding are set forth in Appendix E (infra page 12a) and are found in the Internal Revenue Code of 1954, 26 United States Code Annotated, Sections 162, 177 asd 1221.

STATEMENT

The Proceedings Below

On June 23, 1971, taxpayer (Georator Corporation) filed a complaint against the United States of America to recover income taxes paid. The complaint was filed June 23, 1971 in the United States District Court for the Eastern District of Virginia, Alexandria Division. Taxpayer had, prior thereto, complied with all applicable requirements relative to seeking a tax refund for taxes claimed to have been erroneously assessed and collected.

The United States filed its answer on August 26, 1971.

On April 14, 1972, the parties entered into a stipulation of the issues, substantive facts, procedural matters and submitted the case to the court, sitting without a jury.

And thereafter on October 16, 1972, the Honorable Oren R. Lewis, United States District Judge, entered the Court's opinion, findings of fact and order.

Judgment was entered on October 30, 1972, and the United States of America filed its appeal therefrom.

Facts Established

The trademark "Nobrush" had been adopted by the taxpayer prior to 1952 and has been used continuously in the marketing of electric generators and motors

manufactured by the plaintiff. The said trademark was set forth in a distinctive form and the taxpayer thereby acquired the common law exclusive right to that trademark. Taxpayer has retained and still retains its full common law rights therein.

The taxpayer filed an application for the trademark to be registered on the 29th day of October 1958, and on October 18, 1970, Certificate No. 705,879 was issued by the United States Patent Office.

Taxpayer filed an additional application with the United States Patent Office requesting that its trademark "Nobrush", exclusive of any distinctive method of depicting the same, be placed upon the Principal Register of Marks in the Patent Office. On March 10, 1964, the Patent Office issued Certificate No. 766,253.

The statutory life of the registrations set forth above is 20 years, subject to renewal for an additional period. Such renewal may be denied by the Commissioner of Patents if he finds that certain required conditions have not been met.

On April 20, 1964, the Wincharger Corporation, a subsidiary of the Zenith Corporation, filed in the United States Patent a petition to cancel under 15 U.S.C. 1064(c), registrations of the trademark "Nobrush" alleging that the trademark had become the common descriptive name of an article. The petition was given the numbers 8233 and 8234.

The petition did not challenge or contest any substantive rights of the taxpayer in the trademark and specifically did not challenge the taxpayer's title to the trademark nor the validity thereof, nor taxpayer's entitlement to use the same.

After protracted and costly proceedings in the United States Patent Office, including the taking of depositions by plaintiff and by Wincharger, on February 16, 1968, the Patent Office dismissed the petition because Wincharger had ". . . failed to adduce any substantial evidence to refute the presumptions afforded the involved registrations."

The dismissal by the Patent Office does not bar or estop any qualified party, including the Wincharger Corporation or its successor, from again filing a petition to cancel upon the same grounds, for removal of plaintiff's mark from the Principal Register.

No such actions have been brought against Georator Corporation, since the petition to cancel brought by Wincharger.

As a result of the proceedings in the United States Patent Office, taxpayer narrowed the scope of the registration of said trademark in that the registration indicated that the trade name applied to all motors and generators, but the scope was narrowed so that it applied only to motors and generators without brushes.

On October 2, 1973, the United States Court of Appeals for the Fourth Circuit reversed the case. A Motion for Rehearing was denied on December 26, 1973.

REASONS FOR GRANTING THE WRIT

The errors committed by the Court of Appeals were obviously based on the refusal or failure to distinguish between the acquisition of the trademark and the registration thereof. The overall decision rendered by the Fourth Circuit Court of Appeals was that certain expenditures incurred in the defense by Georator of *its trademark registration* "Nobrush" against attack by

Wincharger Corporation, a subsidiary of Zenith Corporation, should be capitalized and shown on the company's financial records as an asset. The decision would require that the costs of defense would be listed as a capital asset although the expenditure did not result in such a capital asset. It is well established in the accounting practice that any capital expenditure must necessarily result in an asset in order to be a capital item.

The Fourth Circuit Court of Appeals also would establish by its Opinion that successful opposition to a cancellation proceeding by a company against a trademark registration, would be qualified as the same type of expenditure as the cost of the original registration, but defending against one cancellation proceeding would not add any permanent value to the trademark since another proceeding could be filed at any subsequent time either by a different attacker or by the same one.

We seek this writ of certiorari because not only was the Fourth Circuit Court of Appeals in error in its Opinion as a matter of law, but its decision makes impossible proper entries in the records of the companies involved and when the Court of Appeals read into the statute items which were not there, they created a very serious practical problem for accountants of any of the companies holding registrations of trade marks.[1]

The Court's Opinion contains numerous statements which, if accepted as law, make it extremely difficult to classify capital and non-capital items.

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[1] It is believed that there are 450,000 trademark registrations currently existing.

ARGUMENT

We have stated to the Court that the Fourth Circuit Court of Appeals was in error in its Opinion, and to support our position we submit to the Court as follows:

Although the existence of a trademark is a necessary prerequisite to registration, to reverse is not true as a trademark can exist and be fully valid without registration. The registration of a trademark does not create nor confer any additional substantive rights in the trademark, and the registration statute merely recognizes trademark rights which have already been acquired by appropriation. Thus the taxable status of a registration is entirely different from the taxable status of a trademark, but the respondent in this case says they are the same. The petitioner says they are different and supports its position with the following cases:

Huber Baking Company v. *Stroehmann Bros. Company,* 252 F.2d 945, p. 955:

"At this point it is well to consider some general principles of trademark law. Trademark rights are acquired by use, or appropriation, (citing cases) and registration alone of the trademark does not increase the scope of such substantive rights."

Plymouth Motor, 46 F. (2) 211, (C.C.P.A., 1931)

"It is elemental legal doctrine that the Federal Trade-Mark Registration Act substracts nothing from, and makes no addition to, the common-law rights relating to trade-mark ownership and use, except as it furnishes an official forum where owners of marks may have them registered and made public, the machinery for such registration being provided. The act also contains provisions which affect the remedies of an owner in enforc-

ing his or its rights, but in so far as actual ownership of, or rights in, a mark are concerned, these are determined wholly by common-law principles. The weight of authority is to the effect that the statute makes no effort to set up a right of ownership or use, which the common law does not or may not recognize."

Dwinell-Wright Co. v. *National Fruit Produce Co.*, 129 F.2d 848, p. 851

"Registration of a trade-mark under the Trade-Mark Act of 1905 neither enlarges nor abridges the registrant's substantive common-law rights in the mark.

* * * *

Registration, however, does not conclusively establish either a registrant's ownership of the mark, 15 U.S.C.A. Sec. 96, or its validity. 'While it is true that a registered trade-mark cannot be canceled except by direct attack in the way prescribed in the statute, trade-marks registered under the law * * * are not thereby rendered valid. Their validity may still be questioned in any suit in which they are relied upon.' (Citing authorities.)"

Pulitzer Pub. Co. v. *Houston Printing Co.*, 4 F.(2d) 924, p. 926

"[4] This is true of common-law trademarks, and it is equally true of those which have been registered, for the federal Registrations Acts are wholly without effect to extend or limit, except in interstate commerce, as to remedies, the substantive rights which persons have in, or in connection with, those trademarks at comon law. Scandanavia Belting Co. v. Asbestos & Rubber Works, 257 F. 937, 169 C.C.A. 87; Andrew Jergens & Co. v. Woodbury Co. (D.C.) 273 F. 952.

[5] Registration does not create a trademark. It is not essential to its validity. Armour v. Louisville Provision Co. (C.C.A.) 283 F. 42; Phillips v.

Hudnutt, 263 F. 643, 49 App. D.C.! 247, Trappey v. McIlhenny (C.C.A.) 281 F. 23."

Campbell Soup Co. v. *Armour & Co.,* 175 F.2d 795, p. 797

"The trade-mark registration statute expressly confers jurisdiction on federal courts for litigation arising under it. But, on the other hand, federal registration does not create a trademark. The trade-mark comes from use, not registration, and the right to it is in the nature of a property right based on common law."

Pacific Supply Coop. v. *Farmers Union Central Exch., Inc.,* 318 F.2d 894 (1863), p. 905

"[2] Trademark Rights are not dependent on statutory enactment, but arise under common law from prior exclusive appropriation or adoption and use. Piggly Wiggly Corp. v. Saunders, 6 Cir. 1924, F.2d 572."

(The registration of trademarks is provided for in Title 51 USC Annotated, beginning with § 1053, and the Certificates of Registration are provided for in § 1057.)

The respondent, relying on its claim that the taxable status of a registration is the same as the taxable status of a trademark, asserted that the legal expenses incurred in defending the attempted cancellation of a registration was not a business expense but a capital expenditure. That this position is untenable is shown in the following cases:

J. R. Wood & Sons, Inc. v. *Commissioner,* Tax Court Memorandum Decisions, p. 1039

"Reese filed an appeal on the infringement only and the injunction was suspended pending the appeal. The Court of Appeals, Judge Friendly dissenting, reversed as to the injunction on the

ground that there was no likelihood of confusion between 'Artcarved' on the one product and 'Art Crest' on the other. The litigation thus terminated.

The petitioner incurred and paid in the taxable year legal fees in the amount of $15,278.22 in connection with the opposition proceeedings and the infringement suit and claimed that amount as a deduction on its return. The Commissioner disallowed it in full.

* * * *

The deduction in question was incurred in the ordinary conduct of its business in an effort to protect its income and is allowable."

Ditmars v. *the CIR,* 302 F.2d 481, 1962, 2d Circuit, where the attorney's fees in defending a claim against the taxpayer were held deductible as a business expense.

Ursy v. *Price,* where the State Court had ruled in a case before them that title was in the taxpayer *and the legal expenses of the suit had to be capitalized,* but in a second suit, *the legal expenses were properly deductible as a business expense because in the second suit the State Court held that the first decision was res judicata of the title and that the title was not in issue in the second case,* so that the costs of defense in the second suit was a business expense as distinguished from the legal expense in the first case to establish title, which was capitalized. (Cited also in that decision are many cases on point.)

Litigation expenses incurred by a patent owner in an infringement suit are deductible as ordinary and necessary business costs, if they were made in the course of business to protect against infringement and to recover profits and damages. It was held that such expenses could not be appropriately added to the cost

of securing the asset, i.e., patent. *Urquhart* v. *CIR,* C.A. 3d, 215 F.2d 17, 102 USPQ 427.

In another patent case, *Ward* v. *United States,* (D.C. Mass.), 32 F. Supp. 743, the court held that the expense of litigation of patent actions and the subsequent settlement of these actions was not a capital investment but an ordinary business expense, citing *Bliss* v. *Commissioner,* 5 Cir. 57 F.2d 984, and *Kornhauser* v. *United States,* 276 US 145, 48 S.Ct. 219 L.Ed. 505. In the latter case, attorneys fees incurred in the defense of a suit for an accounting were held to be a proper business expense, and thus deductible. These latter two decisions were cited in *Brown-Forman Distillers Corp.* v. *United States,* Ct. of Claims, 132 F. Supp. 711, wherein the court held that if attorneys fees are paid in the 'acquisition' of property, such expense should be capitalized, but if they are paid in the protection of the existing property right, they should be deducted as an expense. In *CIR* v. *Heininger,* 320 US 467, 64 S.Ct. 249, the Supreme Court held that legal expenses incurred in defending a business are "ordinary and necessary" and thus deductible.

While there are distinct differences between patent rights and trademark rights, the cost of enforcing both rights against infringers, i.e., protecting the existing property right, should be considered as "ordinary and necessary" business expenses for income tax purposes.

The case for petitioner is even stronger than indicated by the decisions cited above. In these decisions it was the thing of value itself in issue, namely a patent or other property. *In the instant case, what is being protected is itself a protective device,* one step removed from the asset it protects.

The United States Circuit Court of Appeals for the Fourth Circuit relied in part on *Danskin, Inc.* v. *CIR,* 331 F.2d 360. This case involved the legal expense incurred in the prosecution of a trademark infringement action, the effect of which was to increase the the value of the taxpayer's trademark, and it is true that in that case the Court said that the legal expense constituted a capital expenditure and could not be deducted as a necessary business expense, but the Court explained:

> "The purpose and effect of the legal expenses, as determined by the settlement agreement eventually reached as a result of the litigation taxpayer financed, was to increase the value of taxpayer's registered trademark and to make more secure taxpayer's property in it by forever eliminating the possibility of having it impaired by the competitive use of this confusingly similar mark."

In the case at bar this did not happen. The trademark was not attacked. The property of the petitioner was not endangered, and even if the cancellation had been successful, it would not have affected the common law rights to the trademark. *Pennsylvania Petroleum Company* v. *Pennzoil Company,* 80 F.2d 67, page 70, where the Court said:

> "The proceeding which is now before us is not a proceeding seeking to deprive the appellant of the right to use his trademark. It is a statutory proceeding to cancel a trademark registration which carried with it the prima facie presumption of the exclusive right to use the trademark which had been registered. Our decision, and the decision of the Patent Office, goes no further than to determine that matter."

In *McIlhenny Co.* v. *Gaidry,* 253 F. Rep. 613, p. 617, the Court said:

> "[4] The cancellation, on the opposition of a competitor, of the registration by the defendant's predecessor of the word Tabasco as a trademark under the federal Trade-Mark Act of February 20, 1905 (33 Stat. 724, c. 592 [U.S. Comp. Stat. Ann. 1916, Sec. 9485, et seq.]), does not stand in the way of assertion by the defendant that it has the exclusive right which it claims in this suit. That act, which made provision for the registration of trademarks 'used in commerce with foreign nations, or among the several states, or with Indian tribes, and which conferred certain benefits upon registrants thereunder, did not purport to make registration under it the prerequisite to the acquisition or continued existence of an exclusive right to use a word or symbol as a trademark. If the defendant's predecessor had the exclusive right which the defendant asserts in this suit, that right was not extinguished by the cancellation of the registration mentioned. If the trademark exists, it exists independently of the registration. The cancellation of a registration does not extinguish a right which the registration did not confer. Edison v. Thomas A. Edison, Jr. Chemical Co., (C.C.) 128 Fed. 1013; Capewell Horse Nail Co. v. Mooney, 172 Fed. 826, 97 C.C.A. 248."

We find the Danskin case cited only once, and that in the case of *CIR* v. *Doering,* 2nd Circuit, 1964, 335 F.2d 738, 741, and even then it was suggested that a comparison be made of the Danskin decision with Mertins Law of Federal Income Taxation, Sec. 25A16.

It should also be noted that in the Danskin case a permanent injunction was obtained against a competitor and that litigation in the Danskin case assured the petitioner of an unmolested use of its trademark by the

permanent elimination of competition from a confusingly similar mark. The permanent injunction generated a permanent benefit in respect to an established proprietary right and thereby increased the value of that proprietary right. This is not true of Georator's registrations. There was no permanent injunction, there was no increase in value, and there was no decision which would prevent the bringing of another action exactly the same.

The expenditure of the counsel fees in the case at bar did not produce any income, but it was proximately related to the conduct of the taxpayer's business. It was an expenditure necessary to maintain a property but did not permanently protect it from attack or loss.

In other words, a proceeding to cancel a trademark registration, even if successful, does not affect the registrant's title to or the ownership of the trademark. It involves merely the judicial forum in which the registrant, at some future date, might assert its rights.

Because a registration is so insubstantial a thing, involving the placing of a name on a register and affording certain procedural rights, it is doubtful whether it is capital at all. If it is not a capital item, it is incapable of capital enhancement, as contended by respondent. But even if it is of the nature of capital, it does not follow that an attempt to protect it from cancellation has augmented its value in any way.

It has been stipulated that there was no issue relating to title ownership of the trade mark in the Wincharger v. Georator litigation. Most important is that the petitioner did not defend the cancellation of trademark proceedings in order to protect its right, title or ownership in the trademark, but was merely defending its

right to maintain, if desired, a federal judicial forum in the event there was any infringement of its trade mark.

The Government has always contended that under § 177 of the 1954 IRC, the only way in which the plaintiff could have obtained an amortization of its legal expenses was to comply with the election requirements of said section.

The Court of Appeals' interpretation of § 177 stating that "costs of a cancellation proceeding" is included in the language of the statute is incorrect. Nowhere in § 177 can there be found any language which could be so interpreted. In fact, the section expressly is limited to the acquisition, protection, expense, registration or defense of a trademark, not a defense of a cancellation proceeding, nor is it possible to construe any of the words used in § 177 to include such defense. (See Opinion of Appeals Court, pages 8-9).

In fact a trademark with an indefinite life and no depreciation is not involved in this case. We are dealing with a registration which had a statutory life of twenty years.

In reviewing the legislative history of § 177, we find the Committee saying:

> "Under present law, expenditures paid or incurred by smaller companies in connection with trademarks and trade names such as legal fees are not deductible but must be capitalized. Moreover, such expenditures ordinarily are not amortizable over any period of time since the useful life of most trademarks and trade names is indefinite and not ascertainable. However, certain large cor-

porations are in a position to hire their own legal staffs to handle such matters. Because of difficulties of identification these larger corporations deduct, in some instances, compensation paid to their legal staff for performing the same functions. Smaller companies, however, can not afford to maintain their own legal staff and must acquire outside counsel to perform their legal work. By this amendment your Committee intends to eliminate an existing hardship in the case of small companies."

The Committee in discussing § 177 of the Act of 1954, was referring not to registrations which have a definite life, but to the trademarks and trade names which have an indefinite life. It seems to the petitioner that it was obvious that no one intended § 177 to apply to items with a determinable life span.

CONCLUSION

The petitioner, a taxpayer, seeks this writ of certiorari because he feels that to allow the decision of the Fourth Circuit Court of Appeals to stand would not only be an injustice to it, but would create a definition of a capital asset which would be incorrect and would be a disservice to all Certified Public Accountants and others who are required to determine the nature of an asset.

Respectfully submitted,

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